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No. 91-766

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1991

HERMAN COLEMAN
AND DHIRAJ N. SHAH,

Petitioners,

vs.

CORPORATE RISK MANAGMENT CORPORATION,
MIH CONSULTANTS, INC. AND
MARTIN HOFFMAN,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF OF RESPONDENTS

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QUESTION PRESENTED

WHETHER FORMER STATE OFFICIALS, SUED IN THEIR INDIVIDUAL CAPACITIES FOR THEIR INTENTIONAL OR NEGLIGENT FAILURE TO ACT WHEN ACTION WAS MANDATED BY STATE LAW, ARE IMMUNE FROM SUIT UNDER THE ELEVENTH AMENDMENT AS A MATTER OF LAW?

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BRIEF OF RESPONDENTS

STATEMENT OF THE CASE

From the outset, Petitioners, former Commissioners of Insurance for the State of Michigan, have misrepresented the nature of Respondents' claims against them. They claim this action is a challenge of "their judgment [on] how best to deal with a financially troubled insurance company . . ." and that Respondents seek damages against them individually for actions taken by them which they claim were "within the scope of their official duties." (Petitioners' Brief, p. 7).

However, Respondents are not challenging any discretionary actions or any "judgment calls" made by the commissioners in regard to their dealings with Cadillac Insurance Company. Nor are Respondents challenging actions taken by the commissioners within the scope of their official duties. Respondents seek money damages from the former insurance commissioners, individually, for their failure to take mandatory action in regard to Cadillac Insurance Company immediately when each became aware that Cadillac had violated provisions of the insurance code and Michigan law.

In Michigan, no one may transact insurance business without complying with the Insurance Code of 1956. M.C.L. 500.120; M.S.A 24.1120. Under the Code, the Commissioner of Insurance is charged with the regulation of the insurance business and the execution of the laws in regard thereto throughout the State. M.C.L. 500.202; M.S.A. 24.1202. If it appears to the commissioner that any provision of the Code or any law of the State has been violated, the commissioner must immediately report the violation to the attorney general who will decide whether the facts warrant further action. M.C.L. 500.228; M.S.A. 24.1228.

As previously stated, this action was brought in part against the commissioners for their conduct, while in office, that was contrary to that which was mandated by the Insurance Code of 1956. Specifically, Respondents have alleged:

> 1. Defendants Coleman and Shaw were required by statute to examine the books, records and other documents of all insurance companies incorporated and/or authorized to do business in the State of Michigan, including Cadillac.
>
> 2. Defendants Coleman and Shaw were required, if examination disclosed a violation of the Michigan Insurance Code or the regulations promulgated thereunder, to immediately report the violation to the Attorney General of the State of Michigan.

3. Examination of the books, records, and other documents of Cadillac disclosed, at least as early as 1986, that Cadillac was in violation of certain provisions of the Michigan Insurance Code or the regulations promulgated thereunder with respect to the financial condition of insurance companies incorporated and doing business in the State of Michigan, specifically the requirement of an adequate surplus.

4. Defendants Coleman and Shaw failed to report Cadillac's violations to the Attorney General or to take other steps within their power to prevent Cadillac from continuing to transact business despite its insolvent financial condition.

5. On information and belief, defendants Coleman and Shaw failed to take action with regard to Cadillac's financial condition because of political considerations outside the scope of their offices, and therefore their actions with respect to Cadillac were outside the scope of their authority, were *ultra vires* and were not in good faith.

6. The actions and omissions of defendants Coleman and Shaw with respect to Cadillac amounted to gross negligence or intentional misconduct.

7. In reliance upon Cadillac's apparent good standing as a Michigan Insurance Company and the financial responsibility and/or solvency that this good standing signified, CRM and MIH each engaged in transactions with Cadillac and each expended substantial funds on Cadillac's behalf.

8. To the extent Plaintiffs CRM and MIH are unable to recover from Cadillac the sums owed to each of them, each has been damaged by Defendants Coleman's and Shaw's *ultra vires* and bad faith actions.

(Plaintiffs' Complaint, Docket Entry No. 1, Paragraphs 67-74).

In lieu of an answer, the commissioners moved to dismiss based upon Fed. R. Civ. P. 12(b)(1), 12(b)(6), and 56(b).[1] They argued that *Pennhurst State School and Hospital* v. *Halderman*, 104 S. Ct. 900 (1984), controls this case and "dictates that plaintiffs' claims of impropriety in [their] enforcement of Michigan law cannot be heard in federal court, based on Eleventh Amendment immunity." (Brief in Support of Motion of Defendants Coleman and Shaw for Dismissal, Docket Entry No. 23 p. 8). They argued further that "the statutes which plaintiffs allege [they] have violated grant broad discretion to the Commissioner to take action against an insurance company found to be in financial trouble. Commissioner Shaw and Commissioner Coleman determined in their discretion that Cadillac Insurance Company ought to have an opportunity to rehabilitate itself, to improve its financial condition, before the State took steps to end the Company's existence." *Id.* at 10.

The Honorable Bernard A. Friedman rejected the commissioners' arguments. (*See* Memorandum Opinion and Order, May 16, 1990, in Petitioners' Appendix at 14a-45a). The court first stated that "the eleventh amendment forbids federal courts from hearing claims against state officials or the state itself for violations of state law." *Id.* at 28a. The court then indicated that the Plaintiffs had been sued as individuals and not in their official capacities and that the Eleventh Amendment does not prevent suits against state officials in their individual capacities. *Id.* at 29a.

The court focused next on the criteria for determining whether state officials are individually liable in a given case. *Id.* at 30a. The court said that "Defendants are liable only for actions taken beyond the scope of their authority." *Id.* at 31a. The court then rejected the commissioners' argument that they had broad discretion under the Insurance Code to take action against Cadillac and that all of their actions in this

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[1] The Court addressed the motion only under Rule 12. See Memorandum Opinion and Order, May 16, 1990, in Petitioners' Appendix at 15a.

regard were "within the lawful grant of discretionary authority" for two reasons. *Id.* at 33a. First, the court stated that the statute Plaintiffs alleged the commissioners violated, M.C.L. 500.228; M.S.A. 24.1228, gives the commissioners *no* discretion to decide whether to report violations. *Id.* at 34a. Second, the court stated that Plaintiffs had alleged that the commissioners acted in bad faith willfully or negligently outside of the sphere of their official duties for their own personal, political gain. The court noted that Plaintiffs "might be able to bring forth evidence to show that Defendants acted outside of their official capacities." *Id.* at 34a and n. 5 found at 44a.

The court dismissed the commissioners' motion without prejudice. *Id.* at 37a. The commissioners appealed. A panel of the Sixth Circuit dismissed the appeal for lack of jurisdiction. The commissioners moved for rehearing and the original panel held that a claim of immunity is not appealable when it had been denied without prejudice. *See Corporate Risk Management Corp.* v. *Solomon*, Nos. 90-1713, 90-1730, Unpublished Opinion of the Court of Appeals (6th Cir., Sept. 5, 1991) at 56a. The panel concluded that:

> [d]enials of motions to dismiss on grounds of immunity including Eleventh Amendment immunity are not appealable . . . unless the immunity defense can be decided solely as a matter of law. [Citation omitted]. The immunity defense asserted by the petitioners in the case at bar cannot be decided solely as a matter of law — or at least it cannot be so decided in the petitioners' favor — and the petition for rehearing is therefore DENIED.

Id. at 59a.

The commissoners now seek a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit on the Eleventh Amendment issue. This brief is in opposition to the commissioners' petition.

SUMMARY OF ARGUMENT

Petitioners are former insurance commissioners of Michigan. They have been sued in their individual capacities for certain actions taken while they held public office. The allegations against them are that they willfully or negligently failed to take certain actions state law required them to take. The commissioners claim they are immune from suit in federal court under the Eleventh Amendment. The Eleventh Amendment bars a suit against state officials for a challenge of their discretionary actions; it does not bar a suit against state officials for a challenge of their failure to take action mandated by state law. Therefore, the Petitioners are not shielded by the Eleventh Amendment as a matter of law.

ARGUMENT

I.

THE ELEVENTH AMENDMENT, AS A MATTER OF LAW, WILL NOT BAR A SUIT BROUGHT AGAINST STATE OFFICIALS IN THEIR INDIVIDUAL CAPACITIES FOR THEIR WILLFUL OR NEGLIGENT FAILURE TO TAKE SPECIFIC ACTIONS WHEN STATE LAW MANDATED THOSE ACTIONS TO BE TAKEN.

The commissoners contend that this Court's holding in *Pennhurst State School and Hospital* v. *Halderman*, 104 S. Ct. 900 (1984), applies to this case and, therefore, the Eleventh Amendment shields them from this action as a matter of law. They must claim this for their appeal to have any merit as "denials of motions to dismiss on grounds of immunity including Eleventh Amendment immunity, are not appealable . . . unless the immunity defense can be decided

solely as a matter of law." *Corporate Risk Management Corporation* v. *Solomon*, Nos. 90-1713, 90-1730, Unpublished Opinion of Court of Appeals (6th Cir., Sept. 5, 1991) p. 3 citing *United States* v. *Yonkers Bd. of Educ.*, 893 F. 2d 498, 502 (2nd Cir. 1990). (*See* Petitioners' Appendix at 59a). Their contention, however, is supported neither by fact nor law.

The Eleventh Amendment bars suits against state officials when the state is the real party in interest. *Pennhurst, supra*, at 908. "[R]elief sought nominally against an officer is in fact against the sovereign if the decree would operate against the latter." *Id.* citing *Hawaii* v. *Gordon*, 373 U.S. 57, 58, 83 S. Ct. 1052, 1053, 10 L. Ed. 2d 191 (1963) (per curiam). At this point, the Court noted that "[t]he general rule is that a suit is against the sovereign if 'the judgment sought would expend itself on the public treasury or domain, or interfere with the public administration' or if the effect of the judgment would be 'to restrain the Governmet from acting, or to compel it to act'." *Pennhurst, supra*, at 908 n. 11 citing *Dugan* v. *Rank*, 372 U.S. 609, 620, 83 S. Ct. 999, 1006, 10 L. Ed. 2d 15 (1963) (citations omitted).

Pennhurst involved a class action brought in federal court by mentally retarded citizens of Pennsylvania against Pennsylvania state officials challenging the facts and conditions of confinement in a state institution for the mentally retarded. Specifically, the plaintiffs alleged that conditions at Pennhurst violated federal constitutional and statutory rights as well as rights under state mental health laws.

After trial, the district court found that the conditions at Pennhurst violated each resident's right under constitutional provisions, federal laws and Pennsylvania state law. *Pennhurst* at 904. The district court ordered that immediate steps be taken to remove residents from Pennhurst and that suitable living arrangements be provided for its residents. *Id.* The Court of Appeals affirmed solely on the basis of federal law and remanded the case to the district court for determination of what a suitable living arrangement would be for each pa-

tient. *Id.* The Supreme Court then reversed the judgment of the Court of Appeals, finding that no substantive rights were created under federal law. *Id.* at 905. The Court remanded the case to the Court of Appeals for a determination of whether the order could be supported on the basis of state law, the Constitution or another federal law. *Id.*

On remand, the Court of Appeals affirmed its prior judgment, solely on the basis of Pennsylvania law, without having to reach the issues of federal law. *Id.* The Court of Appeals "rejected petitioners' argument that the Eleventh Amendment barred a federal court from considering this pendant state-law claim." *Id.* The Supreme Court granted certiorari and reversed the decision of the Court of Appeals, holding in part that the Eleventh Amendment prohibits a federal district court from instructing state officials on how to conform their conduct to state law when the state is the real party in interest. *Id.* at 911.

Pennhurst does not support the commissioners' claim of Eleventh Amendment immunity in this case as they would like this Court to believe. Here, both commissioners acted *ultra vires*. The commissioners want this Court to believe that the *ultra vires* doctrine is not a viable exception to sovereign immunity under the Eleventh Amendment. (Petitioners' Brief at 35). "That doctrine excepts from the Eleventh Amendment bar suits against officers acting in their official capacities but without any statutory authority, even though the relief would operate against the state." *Pennhurst*, *supra*, at 915, n. 25. The *Pennhurst* Court questioned the continued validity of the *ultra vires* doctrine in the Eleventh Amendment context but held "that to the extent the doctrine is consistent with the analysis of this opinion, it is a very narrow exception that will allow suit only under the standards set forth in n. 11, *supra*." *Id.*

The standards set forth in note 11 are as follows:

> They [respondents] suggest, however, that the suit here should not be considered to be against the state

> for the purposes of the Eleventh Amendment because, they say, Petitioners were acting ultra vires their authority. Respondents rely largely on *Florida Dept. of State* v. *Treasure Salvors, Inc.*, 458 U.S. 670, 102 S. Ct. 3304, 73 L. Ed. 2d 1057 (1982), which in turn was founded upon *Larson* v. *Domestic and Foreign Commerce Corp.*, 337 U.S. 682, 69 S. Ct. 1457, 93 L. Ed. 1628 (1949). These cases provide no support for this argument. These and other modern cases make clear that a state officer may be said to act ultra vires only when he acts "without any authority whatever." *Treasure Salvors*, 458 U.S., at 697, 102 S. Ct., at 3321 (opinion of STEVENS, J.); accord, *Id.*, at 716, 102 S. Ct., at 3330 (WHITE, J., concurring in judgment in part and dissenting in part) (test is whether there was no "colorable basis for the exercise of authority by state officials"). As the Court in *Larson* explained, an ultra vires claim rests on "the officer's lack of delegated power. A claim of error in the exercise of that power is therefore not sufficient." [Citation omitted]. Petitioners' actions in operating this mental health institution plainly were not beyond their delegated authority in this sense. The MH/MR Act gave them *broad discretion* to provide "adequate" mental health services. [Citation to Pennsylvania law]. The essence of respondent's claim is that the Petitioners have not provided such services adequately.

Pennhurst, *supra*, at 908-909 n. 11.

The majority rejected the dissenting Justices' view that simply an allegation that official conduct is contrary to a state statute would suffice to override the Eleventh Amendment shield. *Id.* The majority's position was that the Eleventh Amendment should prevent a federal court from instructing state officials on how to conform their conduct to state law. That is, the Eleventh Amendment should prevent a federal court from reviewing the adequacy of a state official's exercise

of his discretionary duties. The Court determined that a state official's discretionary actions under state law may not be challenged in federal court. The Court found *Johnson* v. *Lankford*, 145 U.S. 541, 38 S. Ct. 203, 62 L. Ed. 460 (1918), to be consistent with this view. *Pennhurst*, *supra*, at 916 n. 27.

The Petitioners acknowledge that *Johnson* v. *Lankford* is factually similar to this case. (Petitioners' Brief p. 31). In *Johnson*, the plaintiff brought an action against the Bank Commissioner of Oklahoma for his failure to perform his official duties in accordance with state law. The defendants moved to dismiss the action for lack of jurisdiction claiming that the action was one against the state which had not consented to the action, and as such was in violation of the Eleventh Amendment. The plaintiff was a citizen of Massachusetts while the defendants were citizens of Oklahoma.

Johnson had alleged that in exchange for value, an Oklahoma bank, under the control and supervision of the defendant commissioner, executed and delivered to him a certificate of deposit. Approximately 16 months later, the defendant took possession of the bank and its assets due to its insolvency. Thereafter, the plaintiff presented the certificate to the commissioner for payment. The commissioner refused to pay even though by law it was his duty to pay the certificate of deposit at the time it was presented to him. Johnson alleged that the commissioner's refusal to pay the certificate of deposit when it was presented was a gross and entire failure by him to perform his duty. Further, he alleged that the commissioner was aware of the conditions of the bank yet he allowed the persons in charge of it to squander its assets so as to damage plaintiff in his right to compel payment from the bank. He also alleged that the commissioner failed to exercise proper care and supervision in that before the making of the certificate of deposit and thence continuously up to the time he took possession of the bank, he was fully aware that the bank was operating with a reserve that was less than that re-

quired by law and he failed to enforce the law and take possession of it.

The sole question the Supreme Court considered was whether the action was one against the state or against the commissioner as an individual. The Court found that the action was *not* one against the state. *Id.* at 205. The Court said:

> There was certainly no assertion of state action or liability upon the part of the state, and no relief is prayed against it. The charges are all against Lankford. The relief sought is against him because of his willful or negligent disregard of the laws of the state, and it is because of this his surety is charged with liability, it having guaranteed his fidelity.
>
> We think the question, therefor, should be answered in the negative; that is, that the action is not one against the state. To answer it otherwise would be to assert, we think, that whatever an officer does, even in contravention of the laws of the state, is state action, identifies him with it and makes the redress sought against him a claim against the state and therefore prohibited by the Eleventh Amendment. Surely an officer of a state may be delinquent without involving the state in delinquency, indeed, may injure the state by delinquency as well as some resident of the state, and may be amenable to both.

Id. The Court continued by saying that this case was based upon the commissioner's dereliction of duty, "a duty enjoined by the laws of the state, and the dereliction is charged to have been continuous, overlooking violations of the requirements of law by the bank officials by which it was brought to insolvency, knowing of the depletion of its assets, knowing of the reduction of its reserves, and not requiring their repair." *Id.*

Respondents agree with the commissioners that *Johnson* v. *Lankford* is similar to this case. In *Johnson*, the state official

failed to perform duties he was required to perform under the law. In *Pennhurst*, the state officials inadequately performed discretionary duties. The difference between *Johnson* and *Pennhurst* is the difference between *Pennhurst* and this case. Here, there is no question regarding the adequacy of the commissioners' exercise of discretionary duties. The claim against the commissioners is that they failed to perform a duty that was mandated by state law.

M.C.L. 500.228; M.S.A. 24.1228 reads as follows:

> If it appears from any examination made by the commissioner or from any report made to him pursuant to this code, that any provisions of this code or of any laws of the state have been violated, the commissioner *shall immediately report* such violation to the attorney general in writing and the attorney general shall take such action thereof as the facts warrant.

(Emphasis supplied). The statute, by use of the word "shall," mandates action by the Commissioner once he becomes aware of a violation of the insurance code or a state law. The Respondents have alleged that the commissioners willfully or negligently failed to notify the attorney general that Cadillac Insurance Company was in violation of certain state laws immediately when these violations became apparent to them. The statute leaves no room for discretion. The law requires them to act and they willfully or negligently failed to do so.

As in *Johnson*, this action is not one against the state. It is an action against state officials who acted *ultra vires*. Where, as in *Johnson*, a state official willfully or with gross negligence fails to act though his actions are mandated by state law, the Eleventh Amendment does not provide a shield from suit in federal court.

CONCLUSION

Pennhurst does not support the Commissioners' proposition that they should have Eleventh Amendment immunity as a matter of law. In fact, *Pennhurst* supports Respondents' position that the Commissioners' failure to take action that is mandated by state law does not shield them from suit in federal court. Wherefore, as the Commissioners are not immune from suit under the Eleventh Amendment as a matter of law, Respondents respectfully request this Court to deny the Commissioners' Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.

Respectfully Submitted,

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